

Climate change insurance needs

1. Protection gaps and climate change risk

The Chair highlighted that protection gaps and climate change risk remain an ongoing topic at both national and international levels given the impact of recent floods and storms in Europe. It is becoming expensive for insurers to step in to help those suffering damages, but some say that more needs to happen. The panel will focus on how to address this.

2. An outline of the insurance gap out of a still unclear climate related risk landscape

2.1 Transition risk remains the main focus of the insurance sector

An official stated that the community of supervisors unanimously believes that the biggest risk is the transition risk. Insurance groups participating in data collection for the International Association of Insurance Supervisors (IAIS) global monitoring exercise have highlighted that transition risk is difficult to measure and assess. The majority see the situation deteriorating heavily in the next 10 years, making climate risk a top priority for supervisors globally.

2.2 Wide discrepancies exist regarding the insurance gap in the EU

The Chair noted that in Europe insurance coverage levels against natural catastrophes stand at 25%.

An official stated that the extreme weather events in Germany over the past 20 years had each cost on average €1 billion of damage, although the coverage ratio of 52% was good in the European context.

2.3 Insurance gap's actual impact depends on the physical and economic resilience of people, communities, businesses and countries, and their adaption capabilities. Insurance is key to improve the speed of recovery from natural disasters

An industry representative highlighted that climate risk is a consequence of a number of factors including the weather itself, the state of the climate and exposure, and the consequence to the resilience of people and communities. Developing countries are being subjected to changes in weather patterns, so their vulnerability to weather events is very high, alongside little protective infrastructure, tight budgets and zero insurance protection. Globally 45-50% of losses are insured, but in some parts of the world this is 0%. Losses from a natural

disaster can amount to a significant proportion of GDP for small island nation, sometimes over 100%. There is no finance for redevelopment and investing in resilience structures. Every percentage increase in insurance improves the speed of recovery from natural disasters and any protection gap can prevent countries achieving development goals in future years.

2.4 (Re)insurance needs in still transitioning emerging countries are clashing with demanding greening objectives in developed economies

A market expert highlighted the Just Energy Transition Partnership (JETP) between Europe and rice growers in Vietnam as an example of what can be done with all emerging countries. A pool of rural cooperatives are seeking a system of natural catastrophe cover to enable them to export their rice, but this is unaffordable due to the existing system of cap bonds. Local insurance companies seeking cover in Europe are told that capacities have been spent on the remaining European coal electricity infrastructure, which results in macroeconomic risk with demographic and social consequences. The JETP signed between Europe and Vietnam will help transition from coal to renewable electricity and devote part of the funding to reducing the cost of reinsurance. The United Nations Industrial Development Organization (UNIDO) should be involved in such projects.

3. Triggering swift adaption ahead of accelerating natural disasters is a complex challenge

A regulator stated that almost every state in the US has dealt with some form of catastrophic weather event, which impacts financial stability, the economy and the security individuals. Often it leads to access of coverage either people cannot get insurance coverage or afford coverage. Consumers are often confused about what coverage is available and there are gaps in coverage where insurers and reinsurers cannot participate. Some consumers only realize the inadequacy of their coverage after the event once it has happened.

Some catastrophic weather losses can be prevented or at least mitigated. In California, Colorado, and Oregon the wildfires are climate-related and man-related due to a lack of control of vegetation that has created highly combustible situations. In the southeast works to improve building codes will help make buildings more resilient to extreme weather events. There are some states that have developed a high-risk pool where money is collected to help homeowners prepare and become more resilient, making the market fairer and more adaptable.

The Chair commented that an ecosystem is needed to work together to address the issue, so that consumers and communities can find ways to prevent and mitigate risks, and this can be incentivised by insurers.

3.1 Forward-looking risk analysis in this ever-accelerating weather transformation helps adapt insurance undertakings solvency, which in turn contributes to stimulate citizens, communities, and corporates' adaptation

An industry representative highlighted several industry initiatives to integrate climate change into risk assessment models so that insurers can anticipate the reformation of the claims in the future and set aside provisions. The Autorité de Contrôle Prudentiel et de Résolution (ACPR) pilot test, an initiative of 15 insurers, concluded that the risk was a moderate exposure for the industry overall and that claims costs could be multiplied five or six times in certain departments in France.

The digital insurance and long-term risk (DIAL) chair has developed valuation models to estimate the number of potential additional deaths in the case of a heatwave. If the temperature is above 30 degrees for 21 days, with a peak of above 45 degrees, between 7,000 and 20,000 additional deaths are projected. The pilot test was unfavourable to those industries that have the highest greenhouse emissions, because reducing carbon footprint can improve sustainability in the future.

Forecasting and forward-looking models are critical to anticipate what phenomena will happen in the future, enable the verification of the effectiveness of responsible investment policies and take preventative actions.

3.2 Data gaps and capacity building are key challenges for the supervisors globally, to further leverage climate-related scenario analysis for assessing risk

An official stated that scenario analysis is rapidly evolving and an important tool to obtain an assessment of the possible impact of climate risk on insurers' balance sheets. IAIS has been supporting members to conduct climate-related scenario analysis and also to share their experience through workshops. A paper will be published later this year discussing what can be done to support insurers to conduct a climate-based scenario analysis and the more people that contribute the better; assessments can be refined to obtain more relevant results and support good policy decisions.

4. The clarification of climate relate risk would help reinforce reinsurance and cat bonds markets, which are critical for the insurance system in the uncertain context of fast-developing natural events

A market expert highlighted that the protection gap is widening more quickly than the rate of growth of economies, according to The Centre for Risk Studies at

the University of Cambridge. There is a need to reintroduce insurance, especially reinsurance because reinsurance helps to accelerate the recovery of economies to better prepare for new challenges and, in coordination with public authorities, educate the population on risk awareness.

An industry representative concurred that reinsurance is a critical component of the system and that the supply of reinsurance has expanded over the last 15 years. The reinsurance cost was at its lowest ever in 2017 and since has been increasing in price with supply restricting due to the current comparatively inflationary environment. The increase in the frequency of weather events as well as inflation is impacting the cost of recovery.

It is better to invest in data and models, not just on climate, but on the risks themselves. This data is not always reaching the insurers, and so there are many parts of the world in which there may be no information about the types of risks that are being insured. The assets and climate modelling data has to improve to achieve the understanding required to obtain cost-effective reinsurance. Reinsurance pools are being set up in some places in the world to enable cheaper access to reinsurance. For example, the Caribbean Catastrophe Risk Insurance Facility (CCRIF) pools risks to obtain more favourable coverage in the international reinsurance market than could be accessed as individual states.

5. What roles for public authorities, the insurance industry and citizens

The Chair commented that there is clearly a role for public authorities, but also for people. All elements should be part of the solution.

5.1 In a context where natural events make certain risks increasingly uninsurable the first area for cooperation between the public sector, the insurance industry and local communities is to help consumers understand the risk that they are facing

A regulator highlighted that protection gaps continue to widen rather than narrow, occurring where the insurer looks at risk as unsustainable and cannot participate. It is either unaffordable for the customer or they are unaware they need the product. Consumers will buy if they understand the risk that they are facing, and the industry can do a better job informing customers about their need for coverage. Consumers may have an inappropriate understanding that somehow government will come to their rescue when there is a catastrophic event, which it may do to some degree, but never to the extent needed. The NAIC is doing its own catastrophe modelling and data collection to determine where the gaps are in each individual state.

5.2 Avoiding investors and risk carriers leaving the market is essential to better spreading risk. Triggering swift, adequate and pragmatic citizen adaption is key in this respect

A regulator highlighted that industry can be assisted to handle the unsustainable risk by spreading the risk

further with pools of multiple carriers. The more that risk is spread the more it will keep carriers from leaving the market. States are laboratories of innovation because the same thing will not work in every state. In many places there are homes and buildings that would not meet US building codes and therefore not withstand earthquakes, hurricanes, and other catastrophic events.

US Regulators and states focus on making communities more resilient. For example, in South Carolina there is a program to provide grants to fortify their homes. The Strengthen Alabama Homes program helps homeowners retrofit their properties to ensure that building codes are passed and strengthened. The Safe Florida Home programme provides free home inspections, so that people can find out what they can do to fortify their homes. Louisiana and Minnesota have passed mitigation programs. Idaho will attempt to pass a mitigation program using premium taxes from insurance companies, which will allocate a proportion towards making homes more resilient to forest fires.

5.3 Having public and private sector partnerships, enabling or adapting risk, mutualisation or reinsurance schemes is essential

An industry representative explained that the French public and private sector partnership for natural catastrophes created in 1982 allowed for a small amount of money to be set aside from each home policy to go into a general public fund allocated to cover natural disasters. The mutualisation of the fund means that it can be taken advantage of to cover the risk and disaster. It is an excellent system but will need to be adapted in certain elements given the acceleration of climate change and catastrophic events.

France Assureurs has issued an initiative to work on the many challenges that need addressing, including new risks like big fires, clay soil shrinkage and swelling, and which are threatening the fund's ability to pay. The threat of marine submersion and erosion could destroy

up to 1,500 houses in France by the end of the century. Mutualisation is a great approach and there is a need for public and private sectors to work together with customers and supervisors to address the issue and raise prevention awareness.

5.4 Financial support is by far not the sole effort necessary to address insurance gaps; individual risk mitigation and general regulation adaptation are essential

The Chair noted that when EIOPA had looked at the flooding in Ahrtal only 35% of the individuals that had been impacted had insurance, which had led to a discussion about how to insure the houses that had been built back in the same place.

In terms of what else needs to be done at a policy level, an official highlighted the differing roles for the public and private sector. The private sector needs to signal that prevention is key, because loss prevention is effective and a premium should be given if preventative measures are being taken. On the public side it is important to have stricter building codes and, for example, invest in higher buildings on the German coastline.

The Chair agreed that not everything can or will be covered by public money and to do so might be an inefficient system, but there is still a role for public authorities, insurers, consumers, and the worldwide community. EIOPA has published a paper with the European Central Bank that starts with what the individual can do to mitigate, how the insurance sector can help to incentivise and build insurance and reinsurance capacity, and to ensure that there is capital. Risk pooling in a multilateral context can bring public-private partnerships to a national level. The takeaway is that an ecosystem will be needed to deal with this problem, rather than pushing risk to public authorities, which cannot solve this problem alone.